Comments of Harold Furchtgott-Roth[1]

Docket 07-135
November 30, 2010

[1] President, Furchtgott-Roth Economic Enterprises.

I. Introduction

My name is Harold W. Furchtgott-Roth. The current proceeding has a Notice of Proposed Rulemaking in which the Commission considers "whether the current rules governing the tariffing of traffic-sensitive switched access services by local exchange carriers (LECs) are ensuring that rates remain just and reasonable, as required by section 201(b) of the Communications Act of 1934, as amended (the Act)."[2] Tariffs for switched access service are among the last vestiges of rate regulation at the Commission,[3] much of which was swept away by the Telecommunications Act of 1996, to the enormous benefit of the American public. That Act also unambiguously and repeatedly instructed the Commission to deregulate the telecommunications industry and to promote competition. Despite the enormous expansion of competition and advancement of new technologies all to the benefit of the American public, and despite the clear instructions of the Telecommunications Act of 1996 to deregulate and to promote competition, the Commission in this proceeding tentatively concludes to do the exact opposite: to expand regulation of exchange access services offered by local exchange carriers and to stifle competition.[4]

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[2] FCC, *Establishing Just and Reasonable Rates for Local Exchange Carriers*, Docket 07-135, Notice of Proposed Rulemaking, October 2, 2007, at paragraph 1.

[3] Many rules affected by the NPRM date from the 1980s.

[4] The entire language of paragraph 1 frames the NPRM, incorrectly in my view, with a message that additional regulation is necessary:

> In this Notice, we initiate a rulemaking proceeding to consider whether the current rules governing the tariffing of traffic-sensitive switched access services by local exchange carriers (LECs) are ensuring that rates remain just and reasonable, as required by section 201(b) of the Communications Act of 1934, as amended (the Act). In particular, we focus on allegations that substantial growth in terminating access traffic may be causing carriers' rates to become unjust and unreasonable because the increased demand is increasing carriers' rates of return to levels significantly higher than the maximum allowed rate. Although it is reasonable for carriers to seek to increase demand for their services, it is also critical to ensure that rates remain just and reasonable over time as costs and demand change. It has become increasingly important to ensure the reasonableness of rates since the deemed lawful provision in section 204(a)(3) of the Act was adopted because that provision protects unsuspended rates from refund liability. As discussed in detail below, to achieve these goals we tentatively conclude that certain rule modifications are necessary, and we seek comment on those as well as other proposals. [footnotes omitted]

Based on my experience as an economist, a former commissioner of this Commission, and an observer of the telecommunications industry for many years, I have been asked by Northern Valley Communications to offer comments in this proceeding based on the Notice of Proposed Rulemaking.[5]

II. Qualifications

I am president of Furchtgott-Roth Economic Enterprises, an economic consulting firm. I was a commissioner of the Federal Communications Commission ("FCC" or "Commission") from November 1997 through the end of May 2001. In that capacity, I participated in all decisions of the Commission including those affecting access charges for rural telephone companies.

From June 2001 through March of 2003, I was a visiting fellow at the American Enterprise Institute for Public Policy Research ("AEI") in Washington, DC. In 2007, I was a senior fellow at the Hudson Institute, another policy research institute.

I have worked for many years as an economist. From 1995 to 1997, I was chief economist of the House Committee on Commerce where one of my responsibilities was to serve as one of the principal staff members helping to draft the Telecommunications Act of 1996. From 1988 to 1995, I served as a senior economist at Economists Incorporated where I worked on econometric matters in regulatory, antitrust, and commercial litigation cases.

My academic research concerns economics and regulation. I am the author or coauthor of four books: *A Tough Act to Follow?: The Telecommunications Act of 1996 and the Separation of Powers* (Washington, DC: American Enterprise Institute), 2006; *Cable TV: Regulation or Competition*, with R.W. Crandall, (Washington, DC: The Brookings Institution), 1996;

[5] I gratefully acknowledge the financial support of Northern Valley Communications. The views expressed in this paper are my own and do not necessarily represent the views of anyone else.

Economics of A Disaster: The Exxon Valdez Oil Spill, with B.M. Owen, D.A. Argue, G.J. Hurdle, and G.R. Mosteller, (Westport, Connecticut: Quorum books), 1995; and *International Trade in Computer Software*, with S.E. Siwek, (Westport, Connecticut: Quorum Books), 1993. I received a Ph.D. in economics from Stanford University and an S.B. in economics from MIT.

III. Summary of opinions

This proceeding has an extensive record, and I have not benefitted from reviewing all of the documents in that record.[6] Nonetheless, I have read the NPRM as well as many comments in this proceeding. The NPRM and many comments are troubling because they call on the Commission to turn back the clock to a time when regulation of local exchange carriers was the policy prescription to many if not most issues.[7] Times have changed for the better in telecommunications regulation. Today, deregulation and competition are not policy *choices* for the Commission but the *law of the land*.

The remainder of my report is organized as follows:

a. The Commission has yet to explain the compelling need for additional new rules;
b. Even if the Commission were to explain a possible need to consider additional new rules, deregulation and competition are the law of the land, they have proven effective, and they would almost certainly overwhelm any possible consideration of new rules;
c. The specific issues the Commission raises in the NPRM do not compel new rules; and
d. Several important issues are not addressed in the Notice of Proposed Rulemaking.

[6] As of November 18, 2010, at least 527 comments and documents have been filed in this proceeding.

[7] Since the 1980s, the Commission has primarily followed a path of deregulating local exchange carriers. If the Commission were to adopt the tentative conclusions of the NPRM, it would be a rare and unfortunate instance of reregulation by the Commission.

IV. The Commission has yet to explain the compelling need for new rules

For an independent agency such as the Commission under delegated authority from Congress to write new rules that will impose burdens and costs on individuals and companies is not a trivial exercise. The burden to explain clearly the compelling need for new rules falls squarely on the Commission. If the Commission has a compelling need to write new rules with respect to LEC exchange access rates in this proceeding, it has not yet explained it. Indeed, the current NPRM lacks the following:

- a clear purpose with well-defined concepts;
- a clear distinction between lawful and unlawful activities;
- a clear explanation of how the proposed rules would accommodate current market conditions;
- a clear explanation of why current rules are inadequate for the issues posed;
- a clear explanation of how the proposed rules are consistent with existing law and prior Commission decisions; and
- identifiable harms if the Commission fails to take action.

A. The NPRM lacks a clear purpose with well-defined concepts

Although titled "Establishing Just and Reasonable Rates for Local Exchange Carriers," the NPRM is not about either the justness or the reasonableness of rates generally for LECs. The NPRM does not address rates for all services, or even a wide range of services, under all conditions offered by LECs. Instead, the NPRM focuses on just tariffed rates for just one set of services, exchange access services, and a nebulous condition that the Commission has labeled as "access stimulation."[8]

[8] See NPRM, particularly at paragraph 13. Access stimulation is also popularly referred to as "traffic pumping."

"Access stimulation" is central to this proceeding. Without it, one might infer from the NPRM that telecommunications markets would work well. With it, the NPRM implies that markets are dysfunctional. Curiously the NPRM does not define "access stimulation." It is not defined by statute or rule. The NPRM provides little in the way of clear guidance as to what "access stimulation" is, and what it is not. For example, the NPRM states:

> We believe that traffic may be stimulated through a variety of means, including conference bridges, chat line facilities, call center operations, and help desk provisioning. We invite interested persons to comment on the prevalence of these types of operations and to describe in detail how each type of service is provisioned. Interested persons should also identify other types of operations that may result in significant stimulation of access traffic and describe their provisioning arrangements.[9]

These statements almost suggest that "stimulation" is at least partly defined not by any specific characteristic of a LEC or the services the LEC offers but by the services offered by a customer or end user of LEC. "Conference bridges, chat line facilities, call center operations, and help desk provisioning" are not the usual offerings of LECs nor are they necessarily nefarious activities.

The NPRM constructs a framework for new regulations of LECs based not on the characteristics of a LEC but on the characteristics of the service offerings of customers of a LEC. The NPRM frames regulation such that a LEC with one type of customer will be regulated in one manner, but a LEC identical in every way, except with one different customer, will be regulated in a different manner. This approach makes no sense. The Commission regulates carriers, not their customers.

B. The NPRM lacks a clear distinction between lawful and unlawful activities

The distinguishing characteristic that would trigger one form of regulation instead of another under the NPRM is the rate of growth of demand for access services. Although the NPRM disparages the integrity of LECs and their customers with substantial increases in

[9] Ibid.

demand for exchange access services, the Commission does not identify specifically improper services provided by LECs for any, much less all, forms of traffic stimulation.

Nor does the Commission give clear guidance as to a partition between changes in access demand that are "access stimulation" from changes in demand that are not. The Commission even asks how much change in access demand qualifies as stimulation and how much does not:

> Because we find that increased demand beyond some normal traffic growth level will likely result in rates that are unreasonable, we invite interested parties to comment on what an appropriate growth rate would be to trigger a carrier's having to make a new tariff filing, e.g., a 30, 50, or 100 percent growth in demand over the demand used in setting the rates in the currently effective tariff, or over the local switching demand in the same month of the preceding year.[10]

I address this issue in more detail below, but the Commission does not provide clear guidance as to what type of traffic is in need of additional and different regulation, and what traffic is not. A 30% growth rate of traffic per year is substantially different from a growth rate of 100% per year. As I will explain in more detail below, the Commission in neither case clearly demonstrates that traffic that grows at any particular growth rate results in "rates that are unreasonable." The Communications Act does not have language that supports a finding either that a particular growth rate in access demand is unlawful, or that the rates associated with a carrier that has a particular growth rate in demand are "unreasonable." The Commission has had many proceedings on exchange access rates over the past 20 years, but I am not aware that the Commission has previously concluded that the rate of growth of demand is an index of unreasonableness, much less has the Commission partitioned growth rates into realms of reasonableness and realms of unreasonableness. The Commission may attempt to demonstrate some clear and unambiguous causation between growth in access demand and the reasonableness of rates, but at least in the NPRM and in the comments I have reviewed, that causation is not

[10] Ibid., at paragraph 22.

evident. Simply stated, the Commission fails to demonstrate either that increases in access demand are *per se* unlawful or that increases in access demand necessarily lead to rates that are unreasonable and unlawful. At best, the Commission can merely review them on a case-by-case basis, which the Commission may conduct under the current rules.

C. The NPRM fails to explain how the proposed rules would accommodate current market conditions

The Commission in the NPRM fails to explain the current market conditions which are addressed by the proposed rules. For example, in this proceeding, the Commission appears to attribute the growth in access demand to LECs with "incentives and opportunities" and not to their customers.

> With this Notice, we initiate a rulemaking proceeding to examine whether our existing rules governing the setting of tariffed rates by LECs provide incentives and opportunities for carriers to increase access demand endogenously with the result that the tariff rates are no longer just and reasonable.[11]

With a broad brush, the Commission paints the level of demand for access services as an outcome that can be set by LECs "endogenously" in response to "incentives and opportunities." This is a startling observation and one that is not supported by the Commission's own reports which find a consistent and secular decline in the following: LEC access lines,[12] LEC access lines plus VOIP lines,[13] and exchange access service revenues over the past 10 years.[14] Access charge revenues in 2008 were little more than half of their 1998 levels.[15] If the Commission's conclusion in the excerpt were true, one might expect that all LECs would have both the incentive and the capability to choose to have higher demand for access service. The opposite is the case.

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[11] Ibid., at paragraph 11.
[12] FCC, *Trends in Telephone Service*, September 2010, Table 8.4.
[13] Ibid., at Table 8.1.
[14] Ibid., at Table 15.2.
[15] Ibid.

As a result, the Commission in this NPRM seems intent on writing rules that would apply to all LECs, or at least all 61.39 LECs on the assumption that each of those LECs has both the incentive and the capability to will exchange access services to higher levels. The premise makes no sense.

D. The NPRM fails to explain why current rules are inadequate for the issues posed

The NPRM does not explain why current rules for tariffing exchange access services, including the review procedures for those tariffs, are inadequate. As noted above, changes in demand for access services do not meaningfully distinguish between lawful and unlawful activities. One is left with a case-by-case review to determine lawfulness, which is the current rule.

The Commission process of reviewing tariffs on a case-by-case basis does not appear to have revealed a pattern of unreasonable rates in need of new rules. In the three years since this proceeding was initiated, I am aware of only one instance in which the Commission has found a LEC's exchange access rates to be "unreasonable" under Section 201(b) under circumstances remotely similar to those described in the NPRM. That case is under appeal, and the Commission has yet to find any harms from the unreasonable rates.[16] Whether the Commission has found other 201(b) violations or not, no pattern of evidence supports a finding that rates of return for LECs are systematically unreasonable. At least in the NPRM, the Commission has not articulated the need and benefit of replacing existing rules with new and costly rules. Those new rules would impose new administrative costs on hundreds of LECs without supporting evidence that there is any incremental benefit.

[16] FCC, *Qwest v. Farmers*, File No. EB-07-MD-001. The Commission's decisions in that proceeding are under appeal. See *Farmers and Merchants Mutual Telephone Company of Wayland, Iowa v. FCC*, No. 10-1093 (D.C. Circuit, filed May 7, 2010).

E. The NPRM lacks a clear explanation of how the proposed rules are consistent with existing law and prior Commission decisions

The specific issues raised in this NPRM have been addressed in the past by the Commission without a finding of a need for the new and invasive regulations that the Commission now seeks. For example, rules with respect to competitive local exchange carriers (CLECs) were addressed nine years ago.[17] At that time, the Commission specifically rejected the necessity of additional regulation. Now, many years later, and with much more competition in telecommunications markets, the Commission in this proceeding fails to acknowledge that the issues raised in the NPRM have already been addressed, and fails to recognize that the Commission has already decided not to impose additional regulation at least on CLECs. Presumably, the Commission should explain why it now changes its mind, particularly absent any changes in law, any relevant changes in market conditions, or any relevant changes in other circumstances. Telecommunications markets are far more competitive today and in need of less regulation than nine years when the Commission concluded that CLECs needed no additional regulation. The Commission offers no explanation for why more regulation is needed today.

The issue of revising rules for regulation of access charges of CLECs is not new. Indeed, the Commission has examined the same set of issues for many years. The fact pattern is remarkably unchanged, and yet in the NPRM the Commission does not explain what circumstances have changed to cause it to revisit prior decisions. For example, in 2001, the Commission created a rural exemption for small rural CLECs:

> We conclude that the record supports the creation of a rural exemption to permit rural CLECs competing with non-rural ILECs to charge access rates above those charged by the competing ILEC. … Given the role that CLECs appear likely to play in bringing the benefits of new technologies to rural areas, we are reluctant to limit unnecessarily their spread by restricting them to the access rates of non-rural ILECs.[18]

[17] FCC, *Reform of Access Charges Imposed by Competitive Local Exchange Carriers*, Seventh Report and Order and Further Notice of Proposed Rulemaking, Docket 96-262, released April 27, 2001, at paragraphs 65-79.
[18] Seventh Report and Order, at paragraph 65.

The decision to allow rural LECs to charge higher access rates than larger non-rural ILECs was not an accident but a conscious decision:

> The CLECs argue that, lacking the lower-cost urban operations that non-rural ILECs can use to subsidize their rural operations, the CLECs should be permitted to charge more for access service, as do the small rural incumbents that charge the National Exchange Carrier Association (NECA) schedule rates. We note in this regard that a rural exemption will also create parity between the rural CLECs competing with NECA carriers and those competing with non-rural ILECs. [footnotes omitted][19]

The Commission specifically rejected the suggestion that higher access rates were a subsidy to rural carriers. Indeed, the Commission concluded that failing to allow higher access charges would be a subsidy to IXCs:

> In adopting the rural exemption, we reject the characterization of the exemption as an implicit subsidy of rural CLEC operations. It is true that an exemption scheme will permit rural CLECs to charge IXCs more for access to their end-user customers than was charged by the non-rural ILECs from whom the CLECs captured their customers. But that does not necessarily justify limiting the rural CLEC to the access rates of the non-rural ILEC. The same increase in access rates would occur if, rather than entering an area as a competitive carrier, a small local service provider were to purchase a rural exchange and thus become the rural ILEC serving the end users in that exchange. In that event, the IXC's cost for access to the exchange's end users would also increase, as the new ILEC likely would charge either NECA schedule rates or conduct a cost study to support its own access rates, and our rules would permit either outcome. This analysis leads us to conclude that the exemption we adopt today is not properly viewed as an implicit subsidy of rural CLEC operations. Instead, it merely deprives IXCs of the implicit subsidy for access to certain rural customers that has arisen from the fact that non-rural ILECs average their access rates across their state-wide study areas. [footnotes omitted][20]

The Commission correctly observed in 2001 that if claims of perverse incentives were correct, rural America would be filled with new CLECs. That was not true in 2001 and remains untrue today:

> We are also skeptical of AT&T's assertions about the incentives that would flow from a rural exemption. First, AT&T argues that the exemption would "create perverse incentives for uneconomic competitive entry by CLECs in any 'rural' areas in which it might be applicable." It appears from the record that both AT&T and Sprint have routinely been paying for CLEC access billed at the rate charged by the competing incumbent. If AT&T were accurate in its projection about higher access rates spurring a rash of uneconomic market entry in rural areas, such uneconomic entry should already have occurred in the territories of the rural incumbent carriers that charge the higher NECA rates. However, the record fails to indicate such a trend.

[19] Ibid., paragraph 66.
[20] Ibid., paragraph 67.

> Additionally, we note WorldCom's assertion that geographically variable rates will create the incentive for CLECs to make it appear, through "foreign exchange type offerings," as if their end users were located in rural areas when they are not. Here again, it appears that this incentive already has existed for any CLECs that choose to compete with NECA carriers and that consequently would receive the equivalent of NECA rates from Sprint and AT&T. However, the record discloses no significant attempt by CLECs to collect high charges for access to end users that are actually located outside of the NECA carriers' territory.
>
> We are similarly unpersuaded by AT&T's argument that a rural exemption will cause a proliferation of chat line providers in the territories served by rural CLECs. We recognize that AT&T has alleged that, in certain circumstances, it violates the Act for a LEC with relatively high access rates (such as a NECA carrier) to serve a chat line provider as a means of increasing the LEC's access traffic. It appears that the conduct that AT&T challenges in these proceedings grows out of the arbitrage opportunity created by the higher access rates charged by rural NECA carriers. However, we are skeptical that the rural exemption that we create today will add markedly to AT&T's problem in this regard. [footnotes omitted][21]

I provide this extended extract from the Commission's Order to illustrate how the issues and facts before the Commission have changed little in nine years. Yet the Commission now seeks to revisit a decision that it made nine years ago without explaining how facts or circumstances have changed to make a dramatically more invasive and regulatory set of rules necessary.

F. The NPRM fails to explain the harms resulting without new rules

Even if one or more LECs actually had the "incentives and opportunities" to increase demand for access services, the Commission never demonstrates that any specific harm to other parties comes from it. The Commission recognizes that some IXCs complain about access stimulation, but the harm described is limited to potential rates of return for LECs in excess of regulated levels, not direct harm to the IXC or other parties.[22] This issue of course can be addressed under current rules. The entire NPRM in the current proceeding is devoid of any statement of the harms that will ensue if the Commission fails to write new and more restrictive regulations. There is no discussion of harm to consumers, harm to competition, or harm to anyone.

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[21] Ibid., paragraphs 70-71.

[22] NPRM at paragraphs 11 and 12.

Ultimately, the NPRM in this proceeding addresses access stimulation without defining it, without demonstrating that it is unlawful or leads directly to unlawful consequences, or that it harms other parties, or that current rules are inadequate, or that new rules are necessary. Thus, the immediate purpose of the NPRM is unclear, and the Commission has failed to meet its burden to explain the purpose. With these understandings, in Section VI I will address some of the conclusions of the NPRM. But first, it is important to observe that the substantial deregulation and competition in the telecommunications have affected the market for services to reach end users including exchange access services.

V. Even if the Commission were to explain a possible need to consider additional new rules, deregulation and competition are the law of the land, they have proven effective, and they would almost certainly overwhelm any possible consideration of new rules

The experience of the past 15 years, as amply documented by the Commission in its many reports, demonstrates that deregulation and competition have worked. Since the passage of the Telecommunications Act of 1996 and its deregulation of much of the telecommunications industry including particularly local exchange carriers, consumers have more, not fewer, choices for telecommunications services and telecommunications service providers. Consumers have particularly benefitted from the new and innovative services from the least regulated segments of the telecommunications market, the internet and wireless.

The proposal for increased regulation of LECs in this proceeding appears to rest on two incorrect observations: exchange access services are a monopoly; and expanded regulation is required by law and beneficial to consumers. Neither observation is correct.

A. Exchange access service is not a monopoly

Some comments in this proceeding suggest that the Commission should expand regulation in part because exchange access service, particularly terminating exchange access service, is allegedly a *monopoly*.[23] Yet the Commission reveals no evidence in the NPRM or elsewhere that the LECs have market power, much less monopoly power, for exchange access services. Interstate exchange access rates on a per-minute basis declined consistently between 1984 and 2001 not in response to changes in regulation as much as changes in technology and ever increasing competition.[24] By 2010, average total access charges per conversation minute were 1.69 cents for price-cap companies and 5.71 cents for carriers in the NECA pool.[25] The conditions of the telecommunications market are important in the consideration of regulation, but in the telecommunications market, exchange access services are hardly a monopoly.

Moreover, businesses that offer exchange access services likely had little if any market power many years ago and even less likely today. Consumers and businesses have a wide range of alternative means of reaching other individuals and businesses by bypassing exchange access services, and these other means involve far greater traffic and revenue than exchange access services today.

For example, Figure 1 illustrates exchange access services in the mid 1990s for a notional exchange service area served by a LEC and two wireless carriers. End users, z_1, …, z_q, are at the right of Figure 1. These end users may be business customers, residential customers, or any other type of customer or end user. In 1997, competition for interexchange services was relatively robust with several facilities-based carriers, $x_1,\ldots,x_m$ and several resellers, $r_1,\ldots r_n$. Moreover, many wireless carriers, $w_1,\ldots,w_k$ operated in 1997, although relatively few were in any given geographic market.

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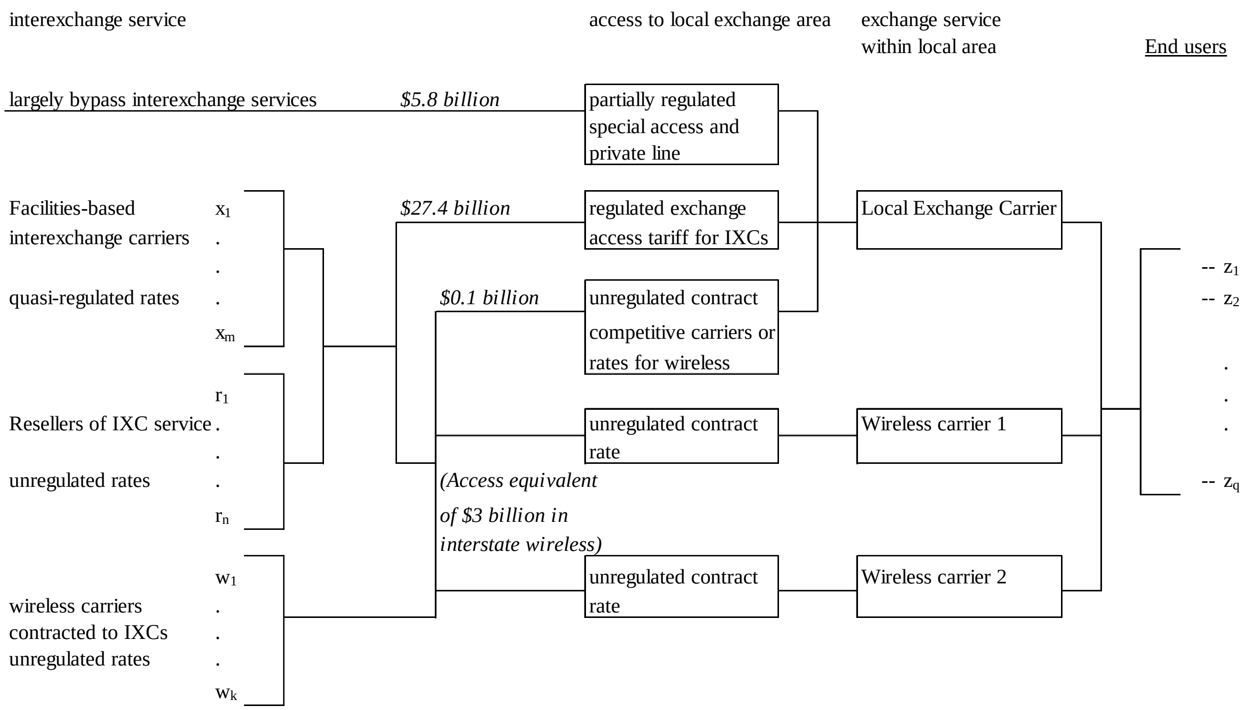
[23] See, e.g., Timothy Tardiff, *The Economics of Access Stimulation: Evaluation of the "Fact Report" by Drs. Alan Pearce and W Brian Barrett (2010), ex parte* submitted by Qwest, August 5, 2010.
[24] FCC, *Trends in Telephone Service*, September 2010, Table 1.2. These values include exchange access services for both origination and termination.
[25] Ibid., at Table 1.4.

Figure 1

Schematic Diagram of exchange access services in 1997
(flows of dollars presented in 2008 dollars)



For the sources for the data in Figure 1, see Table 1 below.

In 1997, these end users on the right-hand side of Figure 1 had effectively just two ways of communicating by voice outside of the local exchange area: through the incumbent LEC (ILEC) or through a wireless carrier.[26] In some markets, end users might also have selected from a competitive access provider (CAP) or one of several nascent CLECs. The access to the outside world in 1997 consisted of several paths. As illustrated in Figure 1, through the LEC, the path could be to the following:

- Quasi-regulated special access or private lines, often used by large companies, that could bypass the traditional long-distance networks. In 1997, LECs had $5.8 billion (in 2008

[26] Consumers had many additional ways to correspond in writing from the U.S. Postal service to emails over the internet. In 1997, voice of internet protocol was in its infancy and not widely adopted; within a few years, VoIP services were ubiquitous.

dollars) in special access and private line revenue, both on the originating and receiving end.[27]

- LECs also interconnected with increasing numbers of competitive LECs and competitive access providers, but in 1997 the access charge equivalent for these competitors was just $0.1 billion.[28]
- Regulated exchange access charges to IXCs. In 1997, these charges amounted to $27.3 billion (in 2008 dollars), by far the most common way of connecting to the outside world by voice.[29] Although tariffed exchange access rates were much higher in real terms in 1997 than today, and although volumes of exchange access services were higher than today for many carriers, the Commission in 1997 did not view exchange access tariffed rates as generally unjust and unreasonable.

Alternatively, end users could connect by voice to the outside world, and vice versa, with wireless devices, primarily cellular phones. By 1997, the wireless industry had grown substantially to reach 55 million subscribers[30] with total revenues of more than $49 billion (in 2008 dollars).[31] Still, in 1997, these wireless operators had only $3 billion in "interstate" services, some portion of which presumably would be equivalent to the exchange access charges.[32] In 1997, most wireless services were local as long-distance wireless services had substantial surcharges.

[27] FCC, "Telecommunications Industry Revenues, 1997," released October 1998, Table 6. The $4.5 billion in 2007 dollars converts into $5.8 billion in 2008 dollars.
[28] Ibid. The reported $110 million in 2007 converts into $141 million in 2008 dollars.
[29] Ibid. The reported $21.3 billion in 2007 converts into $27.3 billion in 2008 dollars.
[30] FCC, *Fourteenth Report on Competition of Commercial Mobile Services*, FCC 10-81, May 20, 2010, Table C-1.
[31] Census Bureau, SIC 4812, at http://www.census.gov/prod/ec97/97s51-sm.pdf. THe $38 billion in 1997 revenue translates into more $49 billion in 2008 dollars.
[32] FCC, *Telecommunications Industry Revenue, 1997*, Released October 1998, Table 7. The reported $2.7 billion in 2007 converts into $3 billion in 2008 dollars.

Altogether, of the charges to provide access to and from local exchange service areas in 1997, the majority, perhaps as much as 80 percent, of those charges were regulated exchange access charges for ILECs. Even so, ILECs did not have a "monopoly" position with respect to controlling access to local exchanges, and the rapid growth of both CLECs and wireless service providers were much anticipated.

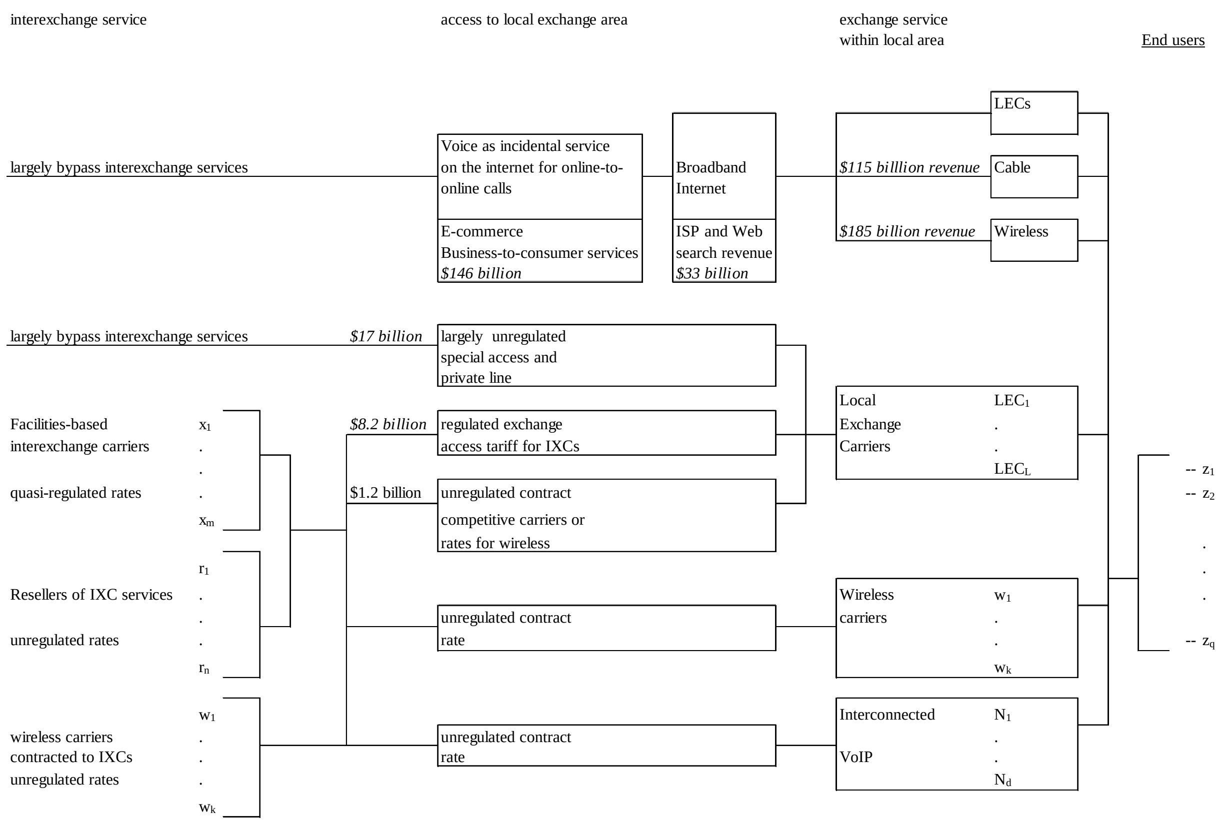
In 1997, methods to bypass local access services for voice communications were available, even if not commonly used. To the extent exchange access services raised antitrust concerns, both federal antitrust agencies had ample opportunities to launch investigations or administrative actions. At that time, the Department of Justice was a frequent commenter on various proceedings at the FCC to deregulate local exchange services and local exchange access services.

By 2008, substantial competition had developed in all areas of the telecommunications market, and tariffed exchange access was a dwindling share both in absolute and relative terms. Figure 2 illustrates the much more competitively robust access for local exchange services in 2008. End users today have many choices both to provide local exchange services and to provide access to those local exchange services. Rather than just one LEC, many end users have a choice of multiple LECs. In addition, end users may choose an interconnected VoIP service, often offered through a bundle with broadband service either through a telephone company or cable operator. In addition, end users have a choice of a wide range of wireless services. In June 2009, 133 million LEC-served end-user switched access lines were in service as well as 23 million interconnected VoIP subscriptions.[33] Of the 157 million wireline end users, 93 million were residential customers and 64 million were business customers.[34]

[33] FCC, "Local Telephone Competition: Status as of June 2009," at 2.
[34] Ibid.

Figure 2

Schematic Diagram of exchange access services in 2008



For the sources for the data in Figure 2, see Table 1 below.

By 2008, regulated tariffed exchange access services had fallen from more than $27 billion to $8.2 billion, and most of those revenues went to one of the Bell Operating Companies.[35] Both tariffed rats and volumes of traffic fell not as a result of regulation but as a result of competition. Revenues for untariffed contract exchange access services were $1.2 billion, presumably primarily connecting LECs with wireless and other unregulated carriers.[36]

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[35] FCC, "Telecommunications Industry Revenues, 2008," released September 2010, Table 5.
[36] Ibid.

The exchange access revenues were overshadowed by special access and private line revenue of $17 billion for wireline companies.[37]

But far more importantly, as illustrated in Figure 2, by 2008 multiple paths were available and widely used effectively to bypass exchange access services for voice and other services. Wireless services and revenues grew rapidly between 1997 and 2008 and continue to grow today. Even more dramatic has been the growth of internet and broadband services. Substantial revenues flow to cable and telephone broadband providers, ISPs, web search engines, and online service providers. For online service providers such as Skype,[38] Google Voice,[39] and Facebook,[40] voice services, conference services, video conference services, and other services are almost trivial add-ons, often free. For many Americans, and quite likely for the vast majority of younger Americans, services that use tariffed exchange access services are not merely bypassed, they are not even considered.

Exchange access charges are shrinking in absolute and relative terms. The notion that exchange access services are a "monopoly" today or even possessing market power is ill-informed. The federal antitrust agencies have the resources, authority, and incentives to protect the American public from the abuse of market power. Both the Department of Justice and the Federal Trade Commission commonly file comments before this Commission. Thus far, neither agency has filed comments in this docket.

Table 1 provides a summary of the changes in revenues for services comparable to local exchange access in both 1997 and 2008. In real terms, exchange access revenue fell by approximately 70 percent between 1997 and 2008. The substantial position of exchange access

[37] Ibid.
[38] http://www.skype.com/intl/en-us/home.
[39] www.google.com/voice.
[40] www.facebook.com.

services in 1997 relative to other forms of access services is also eroded by 2008 when they accounted for less than one-third of such revenues.

Table 1

Changes in Revenue for Services Comparable to Wireline Exchange Access
(in millions of 2008 dolloars)

	1997a, c	2008b
tariff access	27,372	8,206
non-tariff access	141	1,570
private line and special access	5,834	17,041

a FCC, "Telecommunications Industry Revenues, 1997," released October 1998,Table 6.
b FCC, "Telecommunications Industry Revenues, 2008," released September 2010, Table 5.
c Deflated by GDP deflator, at http://www.bea.gov/national/nipaweb

Table 2 presents the range of revenues for various telecommunications-related industries in 1997 and 2008 in constant 2008 dollars. The wireline industry in 1997 was by far the largest, and revenues for wireline telephone companies accounted for approximately 62 percent of the broader telecommunications industry revenue in 1997. Although the data are not necessarily exactly comparable, the $27 billion in tariffed access service revenue in 1997 accounted for approximately 10 percent of wireline industry revenue in 1997 and perhaps 6 percent of the broader telecommunications industry revenue.

By 2008, the overall telecommunications industry had grown by more than 70 percent in real total revenue, but wireline telecommunications revenues declined by 30 percent. Industry growth instead was in cable, wireless, broadband, and online services. Exchange access services were a declining share of a declining segment in the broader telecommunications industry.

Table 2

Change in Revenue for Selected Telecommunications Industries: 1997-2008
(millions of 2008 dollars)

1997 SIC	2008 NAICS		1997	2008
4813	5171	….Wired telecommunications carriers ……………………	279,811	194,765
4812	5172	….Wireless telecommunications carriers (except satellite)	49,154	184,804
484	5175	….Cable and other program distribution ……………………	58,297	115,184
	5173	….Telecommunications resellers ………………………………………...		11,619
	5174	….Satellite telecommunications ………………………………………...		6,925
	5179	….Other telecommunications ………………………………………...		2,218
489		1997 Other telecommunications services	9,064	
	518111	……..Internet service providers ………………………………………...		18,803
	518112	……..Web search portals ………………………………………...		14,370
		Online e-commerce, business-to-consumer services		146,000
7375		1997 Online information services	10,330	
7374	5182	….Data processing, hosting, and related services …………	39,606	77,663
Total telecommunications and selected information services			446,261	772,351

Sources: Census Bureau, 2008 Annual Survey of Service Industries.
1997 Business Census at http://www.census.gov/epcd/ec97sic/E97SUS.HTM.
Bureau of Economic Analysis, GDP deflator, http://www.bea.gov/national/nipaweb
U.S. Census Bureau E-Stats, at http://www.census.gov/econ/estats/2008/2008reportfinal.pdf.

The concept that the exchange access services were a "monopoly" either for originating or terminating calls was in doubt in 1997 and was quaintly anachronistic by 2008. Of course tariffed exchange access services and still applied in 2008, but those services competed with many others.

B. Deregulation is the law of the land

The growth of the telecommunications industry over the past 15 years has reflected both consumer demand and available technology. Extraordinary developments in technology give consumers communications products and services that were unimaginable 15 years ago. This technology is available in telecommunications markets not because the federal government chose to intensify regulation but because it did not. The tenor of communications law for the past 15 years has favored additional deregulation over additional regulation and additional competition over less. The Telecommunications Act of 1996 instructed not once but repeatedly the Commission to deregulate the telecommunications industry. Deregulation is the purpose of the Act in the prologue.[41] Deregulation is the unavoidable outcome of Section 10, in response to petitions from private parties.[42] Deregulation is the inexorable outcome of Section 11, the mandatory periodic review of regulations by the Commission.[43] Deregulation frames Section 204.[44] Deregulation guides Section 706 with respect to broadband services.[45] Deregulation is the refrain of Section 202 with respect to broadcast ownership. Deregulation is the inescapable instruction of the Act.

Deregulation under the Act is not just broad brush strokes but also detailed instructions in specific sections of statute. For example, the Commission is not merely repeatedly instructed to review its rules, but also to end much of pre-existing price regulation,[46] to permit new entrants,[47]

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[41] "An Act to promote competition and reduce regulation in order to secure lower prices and higher quality services for American telecommunications consumers and encourage the rapid deployment of new telecommunications technologies." Prologue, P.L. No. 104-104, 110 Stat. 56 (1996).
[42] 47 U.S.C. 160.
[43] 47 U.S.C. 161.
[44] 47 U.S.C. 204.
[45] 47 U.S.C. 157.
[46] 47 U.S.C. 543.
[47] 47 U.S.C. 253 and 257.

to promote competition,[48] and to remove barriers to providing new services.[49] How strange it is, 14 years after the passage of the Act, to read that the Commission is considering expanding regulation in a manner that will almost certainly create barriers to entry, hobble competition, and discourage the provision of new services.

Many Part 69 rules, particularly those for rural carriers, which are reviewed in this proceeding have not been modified since the early 1980s. Those rules have worked well. By any measure, telecommunications services in rural America have declined in both cost and price, reflect broader national patterns in the diffusion of technology, and are more competitive today than they were in the early 1980s. Any review of these rules today, based on changes in communications law over the past 15 years, would suggest that rules from the early 1980s should either be relaxed or removed in 2010. No foundation in communications law, technology, or the market for telecommunications services would support Commission efforts: to intensify rules for rural carriers, to make those rules more costly to comply with, and to make them more costly for the Commission to enforce. It is extraordinary that the Commission would even contemplate the changes outlined in the NPRM. In the next section, I review some of those changes discussed in the NPRM.

VI. The specific issues the Commission raises in the NPRM do not compel new rules

The Commission discusses several topics in paragraphs 14-38 of the NPRM as possible rationales to expand regulation of exchange access services supposedly in response to alleged access stimulation.[50] I review each of the Commission's topics in turn, and I conclude that in each instance the Commission fails to provide a foundation for expanding regulation. In each

[48] 47 U.S.C. 251-252 and 271-272.
[49] 47 U.S.C. 257.
[50] NPRM at paragraphs 14-38.

instance, competition and deregulation, the current policy framework of communications law, are a better approach than expanding regulation.

A. Just and reasonable rates

In paragraphs 14-17 of the NPRM, the Commission raises the possibility that Section 201(b), apparently on its own and not in conjunction with any other statutory provision, may provide the Commission with a foundation to expand and intensify regulation of exchange access services.[51] These paragraphs represent a substantial departure from the Commission's general policy of deregulation and interpretation of Section 201(b) over the previous 15-20 years. During that time, the Commission has generally deregulated rates and tariff obligations. I cannot recall an instance where the Commission has used Section 201(b) in isolation as a foundation by itself as a pretext to expand regulation. Perhaps the Commission has exercised 201(b) by itself in rare instances, but I believe they are the exceptions rather than the general tendency of Commission policy.

Section 201(b) is not a new statutory provision, but long predates the Telecommunications Act of 1996 and the subsequent deregulatory decisions of the Commission. In those decisions, Section 201 reinforced rather than impeded deregulation. Consequently, Section 201(b) is not antithetical to deregulation by the Commission; it is entirely consistent with deregulation.

According to paragraph 14 of the NPRM, Section 201(b), which requires "just and reasonable rates," "guides the Commission in its review of carriers' rates."[52] A casual reader might infer from this statement that the Commission has an ongoing practice of reviewing

[51] NPRM at paragraphs 14-17.
[52] NPRM at paragraph 14.

carriers' rates, and that each and every rate is reviewed by the Commission as "guide[d]" by Section 201(b). The casual reader would be mistaken.

Many years ago the Commission had a more active role in reviewing tariffed rates. Indeed, the NPRM cites several cases for this observation, all dating from before the Telecommunications Act of 1996.[53] At the time of the cited cases, the Commission regulated not only exchange access rates, but retail long-distance rates, special access rates, and, indeed, rates for practically all forms of interstate telecommunications services. Today, the Commission does little in the way of direct rate regulation, and even exchange access services and to a lesser extent special access services are subject to guidelines and rules, but not specific rate regulation. Tariffed rates can be challenged, and, on occasion, are challenged. The Commission's response to such challenges is not a *de novo* review of the challenged tariff based on 201(b), but more typically a review to determine whether the filed tariff complies with relevant Commission rules.

Paragraph 14 hypothesizes a situation in which demand for exchange access services from a carrier increases dramatically and reaches a startling conclusion that such a carrier, purely on the basis of its access demand characteristics, may have rates that are unjust and unreasonable:

> If, after rates are set, actual demand and expenses differ from the estimated demand and expenses, the realized rate-of-return may be greater or less than the targeted rate of return. The limited information we have suggests that, in certain instances, some LECs are experiencing dramatic increases in demand for switched access services. If the average cost per minute falls as demand grows, the realized rates of return are likely to exceed the authorized rate of return and thus the tariffed rates become unjust and unreasonable at some point.[54]

This excerpt is remarkable for several reasons.

- First the hypothesized conditions are the exception rather than the rule for LECs offering exchange access services. As discussed in Section V above, demand for exchange access

[53] Ibid.
[54] NPRM, paragraph 14.

services over the past 15 years has *declined* dramatically rather than *increased*. For many if not most LECs, tariffed access rates as well as demand for exchange access services were higher in 1997 than in 2008 or today. It does not follow, as the NPRM might suggest, that rates or demand patterns in 1997 were unjust or unreasonable.

- Second, it is impossible that Commission rules with respect to exchange access services and tariffs with respect to those services were necessarily written under assumptions of constant demand. Adjustments are made in the calculation of tariffed rates for changes in demand. That demand for exchange access services would vary is fully anticipated in the rules.[55]
- Third, the observation that for some period of time tariffed exchange access rates might exceed the authorized rate of return is precisely why the Commission requires periodic updates of tariff filings for rate-of-return carriers. The purpose of the periodic updates of the tariff filings is not to find that *prior* rates were "unjust and reasonable" or a violation of Section 201(b), but to ensure that *prospective* rates are proper.
- Fourth, the hypothesized scenario runs exactly counter to the D.C. Circuit Court's opinion in *ACS Anchorage*.[56] In that case, the D.C. Circuit held, Section 201(b) notwithstanding, that Section 204(a)(3) prohibits the Commission from simply going back and reviewing rates after they have been filed. (I discuss this case in more detail below.)

In paragraphs 14-15 of the NPRM, the Commission describes hypothetical scenarios in which a rate-of-return carrier files and tariff and then subsequently has an increase in demand for exchange access services which hypothetically leads to a substantially greater increase in

[55] See various Part 69 rules and 47 C.F.R. 61.39.
[56] *ACS of Anchorage, Inc. v. FCC*, 290 F.3d 403 (D.C. Cir. 2002), No. 01-1059, May, 21, 2002.

revenues than in costs and correspondingly a hypothetical increase in profits, potentially above regulated rates.[57] The Commission seeks comments on these hypothetical situations.[58] I am troubled by the Commission's presentation in these paragraphs for several reasons:

- The hypothetical situation described by the Commission is entirely plausible, but so too are countless other hypothetical situations. The Commission cannot possibly write rules based on every possible hypothetical situation. Section 201(b) instructs the Commission with respect to actual rates applied to actual services under the Act: "All charges, practices, classifications, and regulations for and in connection with such communication service, shall be just and reasonable…"[59] Section 201(b) does not instruct the Commission with respect to hypothetical situations. It does *not* say the following: "All [*hypothetical*] charges, [*hypothetical]* practices, [*hypothetical]* classifications, and regulations for and in connection with such communication service *as [may hypothetically be offered in the future]*, shall be [*determined in advance to be*] just and reasonable…" [Changes to the 201(b) language consistent with the NPRM in italics].
- One might, for example, take the same hypothetical situation described by the Commission but change the parameters with a substantial *decline* in exchange access demand. Does the Commission offer a mechanism to make whole LECs under such situations? I believe, properly, not. Yet these circumstances are common in the industry.
- One might, in another example, take the same hypothetical scenario as described by the Commission but add to it a situation where long-distance carriers engage in self-help and do not pay LECs for tariffed exchange access services. Invoices are sent but not paid. In

[57] NPRM, at paragraphs 14-15.
[58] Ibid., at paragraphs 16-17.
[59] 47 U.S.C. 201(b).

this situation, demand for exchange access services increases substantially, costs increase, but revenues decline or become zero. In this case, marginal revenue is negative.

- Perhaps even more troubling, does the Commission seek to prescribe different regulatory structures on LECs based on different market outcomes that are not known at the time of a regulatory tariff filing? Two identical LECs may file identical tariffs, but they would have different rate structures depending on unforeseeable market outcomes. If that is the direction the Commission seeks to go in, it is taking a profoundly costly and cumbersome regulatory regime and adding layers or complexity and uncertainty to it. The uncertainty would affect not merely the LECs, but also customers—including IXCs—and end users who would not know the rate structure in advance.
- But perhaps most disturbing of all is the Commission's view that the solution to a hypothetical problem is to collect more information and prescribe more complex and cumbersome rules.

The proper solution to these and other problems the Commission may face is less not more regulation.

Ultimately, the problem the Commission addresses in paragraphs 14-17 is whether the Commission should expand regulation of exchange access services in the event of a hypothetical—or even a real—spike in demand for exchange access services for rate-of-return carriers. Ordinarily, in most distribution industries, spikes in demand are beneficial to all distributors at all levels of trade. The spike in demand for exchange access services would likely be viewed positively by everyone as well if all firms had competitive and flexible prices to accommodate changes in market conditions. Many IXCs, however, have fixed rate plans, and most IXCs do not separately itemize for exchange access services.

If instead the IXCs passed the costs of exchange access charges along to their customers, many of the problems claimed by IXCs that are associated with demand for exchange access services would disappear. In particular, IXCs could bifurcate their charges into interexchange services which they provide consistent with 254(g), and separately taxes, fees, and other charges including exchange access service charges which can be itemized and passed along to consumers. Many IXCs already invoice separately for taxes and fees, and access charges could easily be added to the list. To the extent concerns develop with itemizing such charges, the Commission could clarify that such charges are permissible.[60]

Ultimately, the NPRM's discussion of Section 201(b) does not provide either a standalone or a complementary statutory basis to expand regulation of exchange access services, much less an economic basis to expand regulation. The Commission does not explain why current rules are inadequate much less why expanded rules are necessary. The public would be better served, and the Commission would be better advised, if instead of intensifying regulation the Commission were to rely on competition and deregulation to relieve any possible issues raised in this section.

B. Revenue sharing and other compensation

The Commission raises the issue of impermissibility of revenue sharing and other forms of compensation from LECs to third parties.[61] The discussion centers on whether payments to third parties are permissible expenses, and the Commission tentatively concludes that they are not.[62] In contrast, payments to third parties that are not part of the rate base are presumably permissible. The Commission has never previously held such payments to be unlawful. Other

[60] I have long held the view that such separate charges are permissible. See, e.g., Concurring Statement, *In the Matter of Developing a Unified Intercarrier Compensation Regime*, Notice Of Proposed Rule Making, CC Docket No. 01-92, FCC 01-132, April 27, 2001.
[61] NPRM, paragraphs 18-20.
[62] NPRM, at paragraph 19.

regulatory bodies have reviewed issues of payments to third parties and revenue sharing and have not found them to be unlawful.[63]

I do not believe that the Commission has found that revenue sharing violates Section 254(k). [64] The Commission examined 254(k) in the context of *Business Telecom* but did not find a violation, much less one associated with revenue sharing.[65] The Fifth Circuit articulated that 254(k) pertains to the "allocation" of costs, not to the recovery of costs. Section 254(k) thus would seem not to cover issues of revenue sharing.[66]

Revenue sharing arrangements are not uncommon in competitive businesses. When a consumer purchases an iPhone and a wireless service contract from AT&T or another wireless carrier, some of the revenue from the handset and the wireless service contract which is paid to the wireless carrier may ultimately be distributed to Apple, to third-party retail outlets, and to other entities. That a business does not keep all of the receipts that it collects is not an indicator of unlawful or anticompetitive behavior. In the case of AT&T and the iPhone and wireless services, the markets for the services and products provided are quite competitive.

Revenue sharing in the broader communications industry is not limited to either wireless services or handsets. Payphone operators commonly share revenue with location owners. Cable operators pay programmers often directly based on the number of subscribers. Many contracts for competitive services and competitive programming ultimately closely reflect revenue.

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[63] Iowa Utilities Board, *In re High Volume Access Service,* Docket No. RMU 2009-0009, Order Adopting Rules, June 7, 2010.
[64] 47 U.S.C. 254(k).
[65] *AT&T Corp. v. Business Telecom, Inc.; Sprint Communications Company, L.P. v. Business Telecom, Inc.*, Memorandum Opinion and Order, File Nos. EB 01-MD-001 & EB-01-MD-002, May 30, 2001.
[66] *Texas Office Of Public Utility Counsel, et al. v. FCC,* 265 F.3d 313 (5th Cir. 2001) [No. 00-60434, Sept. 12, 2001]. "Section 254(k) concerns cost allocation of joint and common costs, while the SLC and the PICC involve the recovery of such costs. Thus, § 254(k) does not implicate the SLC or the PICC: cost recovery involves how and from whom the funds are collected, while cost allocation refers to how the costs are disbursed." [footnote omitted]

The NPRM's discussion of revenue sharing does not reflect the competitive nature of exchange access and the myriad opportunities that various entities have to reach end users, with or without exchange access services. Nor does the discussion reflect the deregulatory language of the Telecommunications Act of 1996. Even if reaching end users were not competitive, (and of course such access is competitive), and even if regulating payments were not regulatory (which of course such regulation is), regulating fungible payments is extraordinarily difficult. The Commission discusses the "used and useful doctrine," but the citations span the period from 1972 to 1989.[67] The doctrine is still used, but the lack of recent citations illustrates the very difficulty of applying the concept today.

The Commission raises the issue of whether payments to third parties may be *per se* violations of Section 201.[68] The Commission has never taken that position in the past. Section 201(b) refers to charges related to services actually provided, not payments to third parties. If the Commission were to take the irrational view that Section 201(b) prohibits any and all payments to third parties, few if any businesses regulated by the Commission would be immune from scrutiny that some of its expenses may violate Section 201(b).

Many payments to third parties or customers may have essential business purposes and reasonably be part of the cost basis for a tariff. Payments to third parties and customers may be mandated by tariffs, such as for damages associated with accidents or rent to use the land or facilities of another company that happens to be a customer of LEC. In the normal course of business, a LEC has expenditures and makes payments to many businesses in a community served by the LEC. Such payments to third parties are made by all LECs, not just those that are

[67] NPRM at paragraph 19.
[68] NPRM at paragraph 20.

allegedly engaged in some form of access stimulation. Many if not most or all of those businesses will also be customers of a LEC.

Presumably, if the Commission is concerned about payments to third parties, the Commission must clearly distinguish between those payments that are legitimately part of a rate base and those that are not.[69] That distinction is not evident in the NPRM. To implement a program to monitor whether regulated entities make improper payments to third parties would require a substantial expansion and cost of information collection on the part of all LECs and monitoring that information by the Commission.

Perhaps more relevant, the Commission has held that failure by one telecommunications carrier to pay a different telecommunications carrier for service provided can be a violation of Section 201(b).[70]

Ultimately, the NPRM's discussion of revenue sharing and other compensation does not provide either a standalone or a complementary statutory basis to expand regulation of exchange access services, much less an economic basis to expand regulation. The Commission does not explain why current rules are inadequate much less why expanded rules are necessary. The public would be better served, and the Commission would be better advised, if instead of intensifying regulation the Commission were to rely on competition and deregulation to relieve any possible issues raised in this section.

C. Tariff language, access tariff growth rate, and tariff filing issues

The Commission addresses related issues with respect to tariff language, access tariff growth rate, and tariff filing issues in the NPRM.[71] I shall examine each of these in turn, as each

[69] This distinction is relevant only for rate-of-return carriers and not for CLECs.
[70] On this issue with respect to payments to payphone operators, see *Global Crossing Telecommunications Inc. v. Metrophones Telecommunications Inc.,* No. 05–705. 2007.

pertains to a general approach proposed in the NPRM of the Commission imposing a new regulatory regime on the filing of rate-of-return tariffs with mandated updates. Not only is the proposed extent and detail of the proposed new regulations costly and onerous, but the proposal itself runs exactly counter to Section 204(a)(3) and the D.C. Circuit Court's interpretation of it. Section 204(a)(3) states that once a filed tariff has not been challenged within a certain time period, it is deemed lawful in and of itself. The Commission may not subvert a filed tariff by reviewing it *ex post facto*, precisely what the Commission seeks to do in the NPRM. As the D.C. Circuit Court presciently observed in 2002:

> The Commission may have been confused by its pre-s 204(a)(3) habit of retroactively assessing the lawfulness of a rate long after it had taken effect without advance suspension or initiation of hearing. As we noted in our 1995 MCI decision, it is virtually impossible to tell in advance just what rate of return a given rate may yield. 59 F.3d at 1415-16. In a world where the lawfulness of a rate is in almost endlessly suspended animation, the Commission may understandably feel entitled to receive ongoing updates of a company's calculations showing the links between its rates and its rate of return. But that is not the world of § 204(a)(3), where the rate itself, if filed and not suspended, is "deemed lawful."[72]

Yet the repeated effort of the Commission in the NPRM in paragraphs 21-26 is to construct a system of "ongoing updates of a company's calculations showing the links between its rates and its rate of return." In *ACS of Anchorage, Inc. v. FCC*, the D.C. Circuit Court said that what the Commission now seeks in the NPRM is precisely what the Commission is not "entitled to receive." "That is not the world of § 204(a)(3)."

1. Tariff language

The initial tentative conclusion is extraordinary in the economic reach of its inference from a hypothetical example:

> We tentatively conclude that average per minute switching costs do not increase proportionately to average per minute revenues as access demand increases, and that, as a result, rates that may be

[71] NPRM. Tariff language at paragraphs 21. Access tariff growth rate at paragraph 22. Tariff filing issues at paragraphs 23-26.
[72] *ACS of Anchorage, Inc. v. FCC*, 290 F.3d 403 (D.C. Cir. 2002), No. 01-1059, May, 21, 2002.

> just and reasonable given a specific level of access demand may not be just and reasonable at a higher level of access demand.[73]

This is a sweeping statement made without data and one which presumably would apply to any and all switching costs and exchange access services. The Commission is engaged in tentative conclusions that would apply to many carriers in America by mere extrapolation from a hypothetical example. Although subsequent language in paragraph 21 attempts to narrow the scope of this tentative conclusion to certain situations, those limitations are no more factually based than the broad proposition.

The tentative conclusion, based on a hypothetical and rare situation of increased exchange access demand, begs the question of the counterfactual and far more common situation: a decline in access demand. Would the tentative conclusion reach the opposite conclusion under the circumstance of declining access demand that "that, as a result, rates that may be just and reasonable given a specific level of access demand may be [less than] just and reasonable at a [lower] level of access demand."[74]

The Commission is simply not in a position to know the information described in paragraph 21, the detailed marginal revenues and marginal costs of an individual telecommunications carrier at one point in time in one local exchange area, much less for every telecommunications carrier at every point in time at every local exchange area. For the Commission to frame the issue as being dependent on actual marginal revenue and marginal cost information is to set itself up for failure: the Commission cannot possibly know with certainty any of this information, much less all of it. If the Commission must know all of this information to regulate properly, it will never regulate properly.

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[73] NPRM, at paragraph 21.
[74] NPRM, at paragraph 21. Words in brackets altered to fit the alternative circumstance.

The discussion in paragraph 21 is without statutory foundation. Nothing in the Communications Act compels the Commission to collect, much less to rely upon, the information described in paragraph 21 to make regulatory decisions.

Paragraph 21 also does not distinguish between marginal revenue and marginal billing. Billings may increase, but revenues may decrease. Cost structures may increase in any number of ways. The Commission simply asserts that marginal revenues increase more rapidly than marginal costs.

The distinction between revenues and billings is important because many companies that order telecommunications services may delay payments of invoices, or may fail to pay altogether. These and other practices are widely labeled "self-help." The D.C. Circuit Court recognizes that as a general matter the FCC opposes non-payment of invoices and other forms of self-help and prefers that the Section 208 complaint process be used instead to resolve disputes.

> As a rule, grievances are to be raised, as Atlas/Total says, via § 208 and not by resort to self-help. The Commission itself has so stated.[75]

The FCC has made clear that it looks disfavorably on self-help:

> As discussed above, it was made clear at that time that if Frontier believed that a LEC had failed to satisfy its prerequisites to payphone compensation, the IXC was obligated to file a complaint with the Commission to that effect. Instead, Frontier continued to engage in self-help by simply refusing payment without bringing the matter to the Commission for resolution. As has been stated in other contexts, the Commission looks disfavorably on such self-help.[76]

Later in paragraph 21, the Commission appears to misinterpret its responsibilities under the deemed lawful provisions of Section 204(a)(3):

> Thus, the pre-review of the filed tariff, which the Commission identified as its primary means to ensure filed rates are just and reasonable in the *Streamlined Tariff Order*, may not enable the Commission to identify, prior to the time the tariff becomes effective, those cases in which significant increases in access demand will occur after the effective date of the tariff and will result in unreasonable rates. In these circumstances, the deemed lawful provisions would be protecting rates that are unjust and unreasonable rather than protecting customers.[77]

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[75] *AT&T Corp. v. FCC*, 317 F.3d 227 (D.C. Cir. 2003), No. 01-1188, January 24, 2003.
[76] FCC, *Bell Atlantic-Delaware v. Frontier Communications Services, Inc*., 15 F.C.C.R. 7475, p. 9 (2000). Footnotes omitted.
[77] Ibid.

Whether increases in access demand will occur in a few rare instances subsequent to the filing of a tariff has nothing to do with either the *Streamlined Tariff Order* or the deemed lawful provisions. Under no circumstances will the Commission be able to divine in advance the few instances where exchange access demand will increase from the many instances where it will not. Neither lengthier reviews nor more information will increase the Commission's power of omniscience.

The Commission next makes the remarkable statement: "In these circumstances, the deemed lawful provisions would be protecting rates that are unjust and unreasonable rather than protecting customers."[78] Section 204(a)(3) instructs the Commission to provide for the "deemed lawful" status of filed tariffs.[79] Except as specifically prescribed, the statute does not instruct the Commission to fail to provide the "deemed lawful" status of filed tariffs for other causes, even for causes that might arise under other statutory provisions. It is not for the Commission to fail to grant deemed lawful status to a file tariff on the hypothetical possibility that it might someday be "unjust and unreasonable." If the standard is that any tariff that has a rate that might someday be "unjust and unreasonable" cannot receive "deemed lawful" status, then no tariff will receive "deemed lawful" status. Section 204(a)(3) would be vacant of meaning.

Congress instructs the Commission precisely to grant "deemed lawful" status to tariff filings with only prescribed exceptions. If Congress wanted the Commission to have flexibility in granting "deemed lawful" status, it would have given the Commission such flexibility. Indeed, the fact that this prescriptive provision was inserted in the Telecommunications Act of 1996 after the Commission had been receiving filed tariffs for more than 60 years suggests just the

[78] Ibid.
[79] 47 U.S.C. 204(a)(3).

opposite: Congress does not want Commission to exercise any discretion or flexibility in granting deemed lawful status to filed tariffs. The Commission may harbor its own views about whether the deemed lawful provisions "would be protecting rates that are unjust and unreasonable rather than protecting customers" but those views are completely irrelevant to the Commission's statutory obligation to follow 204(a)(3).

From its misreading of Section 204(a)(3), the Commission makes another striking tentative conclusion:

> We tentatively conclude that the Commission should have the opportunity to review the relationship between rates and average costs through the filing of a revised tariff when a section 61.38 or 61.39 carrier experiences significant increases in traffic to ensure that just and reasonable rates are maintained.[80]

Of course, this conclusion is contrary to Section 204(a)(3) and to the findings of the D.C. Circuit Court in *ACS Anchorage*. The Commission moreover segregates Section 61.38 and 61.39 carriers from other carriers and requires them to file different types of tariffs from other carriers. The Commission is concerned about only one type of change in circumstances—exchange access services, and changes in only one direction, substantial increases. Under most common carrier precedents, the timing and frequency of tariff filings are largely at the discretion of the common carrier. Under the Commission's proposal, the filing of tariffs will be at the discretion of the regulator, and the regulator will require more frequent filings from one class of carriers and not others.

The Commission goes further and tentatively concludes that specific language in tariffs from Section 61.38 and Section 61.39 is necessary:

> If the monthly local switching minutes of the issuing carrier exceeds [__] percent of the local switching demand of the same month of the preceding year, the issuing carrier will file revised local switching and transport tariff rates to reflect this increased demand within [__] days of the

[80] NPRM at paragraph 21.

end of that month.[81]

Aside from the dubious value of the micromanagement of the tariff process, it is worth noting that the Commission addresses traffic but does not address revenue. Hypothetically, traffic might increase 10-fold for a LEC but revenue might decline to zero. Under these circumstances, it is difficult to see who would benefit from the filing of a new tariff.

2. Access tariff growth rate

The NPRM seeks comment on the appropriate level of growth in exchange access demand to trigger the filing of a new tariff under the construct in the previous subsection.[82] The Communications Act gives no direction to the Commission to regulate on the basis of changes in demand for access services nor any instruction to discourage growth of access services. Indeed, it is not obvious why the Commission should not be encouraging growth of access services, particularly given that they are in decline.

Moreover, it is striking that the Commission focuses on growth of demand for access services rather than access service revenue. As noted above, substantial differences between changes in demand for services and changes in revenues. To the extent the Commission is truly concerned about marginal revenue, then changes in revenue would appear to be a better proxy than changes in demand.

Perhaps the most peculiar issue raised in this subsection by the Commission is forbearance:

> If such a rule is adopted, parties should address whether the Commission should forbear from applying deemed lawful status to the new tariff rates.[83]

The NPRM frames forbearance incorrectly. See Subsection E below.

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[81] Ibid.
[82] NPRM at paragraph 22.
[83] Ibid.

3. Tariff filing issues

The NPRM addresses tariff filing issues.[84] The first few paragraphs address the details of tariff filing under the triggering mechanism discussed above. The NPRM presents the following tentative conclusion:

> We tentatively conclude that the average schedule formulas can only yield reasonable estimates of an average schedule carrier's cost when the demand is within the range used to develop the formulas. When an average schedule carrier experiences a significant growth in demand that takes it outside the observed range of demand used to establish the average schedule formulas, the process of running the increased demand data through the formulas produces what appear to be extreme increases in costs for the carrier. This increase appears to be inconsistent with the efficiencies carriers would be expected to realize as access demand increases.[85] [footnotes omitted]

Leaving aside the general limitations of any model to estimate the costs of any firm, it does not necessarily follow that all cost models are always calibrated for a specific range of demand or that the precision of the estimates of cost models is knowable in different ranges of demand. I do not believe that most average schedule formulas used in tariff filings have the statistical properties consistent with the NPRM's tentative conclusion. It is one matter either to be skeptical generally about the accuracy of a cost model or to suspend disbelief about the accuracy of a cost model. It is an entirely different matter, and I believe less defensible, to suspend disbelief for one range of demand yet to be skeptical in another range of demand. The accuracy of costs models is not based on an on-and-off switch.

Ultimately, the NPRM's discussion of tariff language, access tariff growth rate, and tariff filing issues does not provide either a standalone or a complementary statutory basis to expand regulation of exchange access services, much less an economic basis to expand regulation. The Commission does not explain why current rules are inadequate much less why expanded rules are necessary. The public would be better served, and the Commission would be better advised,

[84] NPRM at paragraphs 23-28.
[85] Ibid. at paragraph 25.

if instead of intensifying regulation the Commission were to rely on competition and deregulation to relieve any possible issues raised in this section.

D. Certification

The NPRM examines a possible certification for 61.39 tariff filers that they are not engaged in "traffic stimulation."[86] The NPRM never clearly defines traffic stimulation, and it seems implausible that carriers can certify not to be engaging in an activity which the Commission itself cannot define. The Commission clearly is aware of the lack of a clear definition:

> Parties should address how they would define traffic stimulation for purposes of such a certification. Since some form of enforcement action outside the tariff review process appears to be contemplated, a clear delineation of what is objectionable traffic stimulation is necessary to avoid inadvertently penalizing carriers engaging in legitimate activities due to ambiguous rules. For example, it is not clear that merely saying traffic increased by some percentage, without looking at the reasons for the increases, would be adequate.[87]

This excerpt from the NPRM captures the Kafkaesque nature of the proposed regulation: The Commission seeks to regulate something; the Commission cannot define it; the Commission seeks carriers to certify that they are not engaged in this activity; yet the Commission recognizes that it may be "inadvertently penalizing carriers engaging in legitimate activities due to ambiguous rules."

It is little comfort—indeed, it is a source of great discomfort—that the Commission must look at the "reasons for the increases" to determine if traffic increases are lawful or not. All of this puts the Commission in the uncomfortable position of examining the content and the users of telecommunications services and making a judgment about whether they are good or bad. Much has been said about *network neutrality* and the notion that telecommunications carriers and broadband service providers should not discriminate based on the identity of a user or the content

[86] NPRM at paragraph 27.
[87] Ibid.

of programming. Yet in this NPRM, the Commission appears to be making a judgment that whether growth in exchange access services has merit or not depends at least in part on "the reasons for the increases."

If the Commission does promulgate rules, it would likely be in the awkward position of enforcing rules for an activity it cannot define and punishing carriers which have done no wrong, All carriers will be punished through higher costs of complying with additional burdensome regulations.

Ultimately, the NPRM's discussion of certification does not provide either a standalone or a complementary statutory basis to expand regulation of exchange access services, much less an economic basis to expand regulation. The Commission does not explain why current rules are inadequate much less why expanded rules are necessary. The public would be better served, and the Commission would be better advised, if instead of intensifying regulation the Commission were to rely on competition and deregulation to relieve any possible issues raised in this section.

E. Possible forbearance

The NPRM devotes an entire section to the improper consideration of forbearance from Section 204(a)(3).[88] As the Commission itself noted in implementing Section 204(a)(3), it is part of the deregulatory design of the Telecommunications Act of 1996:

> On February 8, 1996, the "Telecommunications Act of 1996" (1996 Act) became law. The intent of this legislation is "to provide for a pro-competitive, de-regulatory national policy framework designed to accelerate rapid private sector deployment of advanced telecommunications and information technologies and services to all Americans by opening all telecommunications markets to competition." This Report and Order adopts rules to implement section 402(b)(1)(A)(iii) of the 1996 Act, which adds section 204(a)(3) to the Communications Act. This section provides for streamlined tariff filings by local exchange carriers (LECs).[89]

[88] NPRM at paragraphs 29-30.
[89] FCC, *Implementation of Section 402(b)(1)(A)of the Telecommunications Act of 1996*, Report and Order, 97-23, January 31, 1997, at paragraph 1.

According to the Commission, Section 204(a)(3) is a deregulatory provision, presumably not a provision from which the Commission could subsequently choose to forbear for the purpored purpose of additional deregulation.

As noted above, Section 204(a)(3) is a deregulatory provision that removes from the Commission the *discretion* to withhold deemed lawful status to a filed tariff after certain dates.

> Any such charge, classification, regulation, or practice shall be deemed lawful and shall be effective 7 days (in the case of a reduction in rates) or 15 days (in the case of an increase in rates) after the date on which it is filed with the Commission unless the Commission takes action under paragraph (1) before the end of that 7-day or 15-day period, as is appropriate.[90]

The Commission specifically considered, and rejected, the possibility that under Section 203 the Commission could defer consideration of a tariff filing beyond the statutory language of 204(a)(3):

> We conclude that the more recent and specific provisions of the 1996 Act take precedence over our general deferral authority in section 203. We believe continued application of the general deferral authority contained in section 203 to LEC tariffs filed on a streamlined basis under the specific provisions set out in new section 204 (a)(3) would be contrary to Congressional intent. Accordingly, we adopt our tentative conclusion in the Notice that we may not defer LEC tariffs filed under the tariff streamlining provisions of the 1996 Act.[91]

The Commission also considered, and dismissed, the concept that some LEC tariff filings would not be subject to streamlined consideration:

> We find that all LEC tariffs involving rate increases, decreases, and/or changes to the rates, terms, and conditions of existing services are eligible for streamlining. We also conclude that LEC tariffs introducing new services are eligible for streamlined filing. Making all LEC tariffs eligible for streamlining will provide a consistent reading of section 204(a)(3) and section 204(a)(1) by establishing that all tariff filings are subject to the provisions of section 204. We agree with NYNEX that we have consistently interpreted section 204(a)(1) as giving the Commission authority to investigate and impose an accounting order on all types of tariffs, including those for new services. Making all LEC tariffs eligible for streamlining will continue this practice as well as give greatest effect to Congressional intent to streamline the LEC tariff process. In addition, we find that this interpretation will simplify the administration of the LEC tariff process by making it unnecessary for the Commission, carriers, or interested persons to determine whether a particular tariff qualifies for streamlining. Accordingly, we determine that all LEC tariffs are eligible for streamlined filing.[92]

[90] 47 U.S.C. 204(a)(3).
[91] FCC 97-23, paragraph 6.
[92] FCC 97-23, paragraph 31.

The Commission made no exceptions based on any consideration including the possibility of changes in demand for exchange access services or changes in any other market condition. The Commission under Section 204(a)(3) does not admit a form of discrimination among tariff filings whereby some tariffs are treated in one manner and others are treated in a different manner.

The Commission considered and rejected the notion of screening tariff filings to reject some as facially impermissible. It decided against such an approach:

> We will not establish presumptions of unlawfulness for any categories of tariffs. Such presumptions would be inconsistent with the legislative intent of this provision.[93]

Section 10 is intended to allow the Commission to apply less regulation, not to create more regulations or to apply more stringent regulation.[94] The Commission has considered the interaction between Section 10 and Section 204(a)(3), and the Commission concluded that Section 204(a)(3) would not preclude the Commission from detariffing LECs under Section 10.

> We affirm our tentative conclusion that we may exercise forbearance authority to reduce or eliminate tariff filing requirements for LECs, including the filing of tariffs eligible for streamlined treatment. … Absent any express limitation on our authority to forbear from applying tariffing requirements of section 203 of the Act, we conclude that we have authority to do so under section 10(a). In addition, we find it difficult to construe section 204(a)(3), which states that LECs "may" file streamlined tariffs, and our section 10 forbearance authority to mean that the statute imposes a requirement that LECs "must" file tariffs. Rather, we find that Congress intended to reduce or eliminate regulation as competition develops and to provide for the detariffing of LEC services under appropriate conditions.[95]

In the current NPRM, the Commission did not clearly articulate how Section 10 could apply to Section 204(a)(3). To deregulate further under Section 204(a)(3) might possibly mean to grant deemed lawful status immediately without review. Any extension of the time of regulatory review, or any withholding of deemed lawful status would be the expansion of

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[93] FCC 97-23, paragraph 61.

[94] 47 U.S.C. 160. Section 10 instructs the Commission to "forbear from applying any regulation or any provision of this Act to a telecommunications carrier…"

[95] FCC 97-23, paragraph 37.

regulation, and not a plausible outcome of Section 10. Moreover, of the triggering mechanisms for Section 10 review, two refer to "enforcement of such … provision is not necessary …" and the third refers to public interest and the promotion of competitive markets.[96] The only plausibly outcome of failing to enforce the provisions of Section 204(a)(3) would be the immediate granting of deemed lawful status. Not granting deemed lawful status within the prescribed time would be expanding regulation under 204(a)(3), not deregulating. Such expansion of regulation would not enhance competition but would deter competition as potential competitors for telecommunications services would view regulation as lawless and unpredictable.

Ultimately, the NPRM's discussion of forbearance does not provide either a standalone or a complementary statutory basis to expand regulation of exchange access services, much less an economic basis to expand regulation. The public would be better served, and the Commission would be better advised, if instead of intensifying regulation the Commission were to rely on competition and deregulation to relieve any possible issues raised in this section.

F. Competitive LECs

The Commission addresses the possibility of "traffic stimulation" by rural competitive LECs.[97] It would be a substantial departure from most Commission precedents to impose new and onerous regulations on CLECs. Verizon proposes that rural CLECs file quarterly reports.[98] The Verizon proposal would create a substantial filing burden on rural CLECs. This approach would also be a radically different interpretation of Section 204(a)(3) with discriminatory treatment rural CLECs instead of the non-discriminatory treatment of filed tariffs in the past. In general, the discussion in the CLECs in paragraphs 34-37 anticipates a different set of rules for rural CLECs under 204(a)(3) than for other carriers. As the Commission correctly concluded in

[96] Ibid.
[97] NPRM at paragraphs 34-37.
[98] NPRM at paragraph 35.

1997, it is incorrect to read Section 204(a)(3) as applying differently to any set of LEC tariff filings. It is particularly difficult to see how the provision could be interpreted to apply differently to rural LECs generally, and differently between rural ILECs and rural CLECs. The possibility of such an outcome is not to be found in the statutory language.

Ultimately, the NPRM's discussion of CLECs does not provide either a standalone or a complementary statutory basis to expand regulation of exchange access services, much less an economic basis to expand regulation. The Commission does not explain why current rules are inadequate much less why expanded rules are necessary. The public would be better served, and the Commission would be better advised, if instead of intensifying regulation the Commission were to rely on competition and deregulation to relieve any possible issues raised in this section.

VII. Several important issues are not addressed in the Notice of Proposed Rulemaking

Several issues that would have been appropriate to address in the NPRM were omitted. These include the following:

- Benefits to consumers of a wide range of choice of services;
- Barriers to entry and discouraging new services;
- Effect of access stimulation on other segments of the telecommunications industry;
- Self-help by refusal to pay invoices;
- Mandating discrimination among end-users;
- Obligations to rural America; and
- A deregulatory solution.

I review each of these topics in turn.

A. Benefits to consumers of a wide range of choice of services including "free" options

This proceeding is entitled "Just and Reasonable Rates for Local Exchange Carriers," but it should also consider the choices available to consumers in the market. Many services possibly associated with "access stimulation" clearly are lawful and clearly benefit consumers. For example, when a call center is opened in a local exchange area and substantial increases in exchange access follow, neither consumers nor the public is harmed. Like all consumers, Americans prefer lower prices to higher prices, and "free" is best of all. When consumers call "free" conference calling services, consumers are not harmed. Indeed, when consumers voluntarily place calls to any service that the Commission associates with "access stimulation," the consumer is not harmed. No one compels a consumer to make a call to a number that may be part of "access stimulation."[99]

To the American consumer, "free" is an attractive offer. "Free" is widely used lawfully to attract and retain customers. Some IXCs and wireless carriers properly offer "free" evenings and weekend services. Some wireless carriers offer "free" handsets. Some LECs offer "free" vertical services. If, as a result of these and other "free" offers, demand for IXC and wireless services increases on evenings and weekends, the fact pattern is not one of unlawful "access stimulation." The result instead is the natural ebb and flow of competitive markets, with firms seeking every opportunity to remain viable and competitive in the market. The Commission should marvel at the workings of competitive markets rather than seeking to interfere with them.

No doubt, some services accessible by phone are harmful for moral or ethical or criminal reasons. But these harms to consumers based on the type of programming accessed or the activity conducted on the phone are related to the *conduct* of the consumer, not to the nature of

[99] I am addressing situations only where demand for exchange access services is the result of individuals making calls.

the underlying telecommunications service, whether based on “access stimulation” or not. The underlying problem of individuals seeking pornography on a phone is the pornography, not the structure of exchange services for the phone call. Of course, most harmful and illegal content are more readily available through the internet than through a voice call on the public-switched network. As described in Section V, the vast majority of traffic and traffic growth are on the internet.

B. Barriers to entry and discouraging new services

The Commission is instructed to remove barriers to entry of providing new services.[100] Some new and innovative services may be associated with characteristics that the Commission might associate with “access stimulation.” The rules proposed in the NPRM would create barriers to entry and discourage the development of new services that require a rapid increase in demand for exchange access services. The possible adverse consequences of the proposed rules for new services and for new service providers are not addressed in the NPRM.

C. Effect of access stimulation on other segments of the telecommunications industry

Although the NPRM implies that access stimulation financially harms parts of the telecommunications industry, particularly IXCs, I am not aware of any verifiable empirical evidence. The NPRM offers none, and the comments in this proceeding do not appear to have presented any credible evidence. TEOCO, for example, has a study which purports to measure hundreds of millions of dollars of losses annually from access stimulation.[101] The study, however, is entirely undocumented. I have not seen anything in the record in this proceeding to document the losses for any IXC, and the TEOCO study has no credibility. One of the many deficiencies of the TEOCO study is that “traffic pumping” or “access stimulation” is not

[100] 47 U.S.C. 257.
[101] Available at: http://whitepapers.ccmi.com/WhitepaperSummary.aspx?whitepaper_id=116.

precisely defined. The TEOCO calculations are not only undocumented, but it is unclear what losses the study is attempting to measure.

If the damages claimed by TEOCO were true, one would expect that one or more of the IXCs would have annual losses of one hundred million dollars or more from access stimulation, and that those losses would be reflected in the company's public reports to the SEC. I have reviewed the Form 10-Ks for several large IXCs. Sprint and Qwest mention "traffic pumping" but only in the context of possible regulatory outcomes. Qwest discloses that regulatory or judicial outcomes with respect to access stimulation may have a "material adverse effect" on Qwest.[102] Sprint, on the other hand, claims that FCC decisions may have an unspecified "direct beneficial impact" on Sprint.[103] No mention is made by either Qwest or Sprint of any specific losses from access stimulation. AT&T and Verizon, by far the two largest IXCs, do not mention

[102] See Qwest Communications International Inc., Form 10-K, for period ending 12/31/2009, filed February 16, 2010, at 15:

> Also under review by the FCC and state commissions are the intercarrier compensation issues arising from the delivery of traffic destined for entities that offer conference and chat line services for free (known in the industry as "access stimulation," or "traffic pumping")…There can be no assurance that future regulatory, judicial or legislative activities will not have a material adverse effect on our operations, or that regulators or third parties will not raise material issues with regard to our compliance or noncompliance with applicable regulations.

[103] See Sprint Nextel Corp, Form 10-K, for period ending 12/31/2009, filed February 26, 2010, at 10-11:

> The FCC currently is considering measures to address "traffic pumping" by local exchange carriers (LECs) predominantly in rural exchanges, that have very high access charges. Under traffic pumping arrangements, the LECs partner with other entities to offer "free" or almost free services (such as conference calling and chat lines) to end users; these services (and payments to the LECs' partners) are financed through the assessment of high access charges on the end user's long distance or wireless carrier. Because of the peculiarities of the FCC's access rate rules for small rural carriers, these LECs are allowed to base their rates on low historic demand levels rather than the vastly higher "pumped" demand levels, which enables the LEC to earn windfall profits. The FCC is considering the legality of traffic pumping arrangements as well as rule changes to ensure that rates charged by LECs experiencing substantial increases in demand volumes are just and reasonable. As a major wireless and wireline carrier, we have been assessed millions of dollars in access charges for "pumped" traffic. Adoption by the FCC of measures to limit the windfall profits associated with traffic pumping would have a direct beneficial impact on us. Recent positive decisions against several LECs and their traffic pumping partners in U.S. district courts and before the Iowa Utilities Board and the FCC may result in some decrease in this activity.

access stimulation at all, much less losses from it.[104] Centurylink, which is acquiring Qwest does not mention access stimulation either.[105] None of the IXCs reports any losses associated with long-distance voice calls.

The Commission publishes data on average revenue for IXCs for interexchange calls, even net of access charge payments, Universal Service Fund fees, and other charges.[106] These data consistently show revenue of several cents per minute even net of these charges and are always substantially greater than most exchange access rates. Although the Commission does not report marginal revenue rates, the average rates do not reveal a systematic problem leading to losses for IXCs.

D. Self-help by refusal to pay invoices

Although this proceeding is entitled "Just and Reasonable Rates for Local Exchange Carriers," rates have little meaning if invoices are unpaid. Some IXCs increasingly delay or avoid payments of access charges to LECs, both with and without allegations of access stimulation. Not addressed in the NPRM, this issue is closely tied to the concept of just and reasonable rates. In a separate but related proceeding, the Commission has held that failure to pay payphone service providers is a violation of Section 201.[107] The Supreme Court upheld that position.[108] In the NPRM, the Commission presents several proposals to lead to what purportedly would be more "Just and Reasonable Rates for Local Exchange Carriers." None of these proposals would increase the certainty of payments to LECs for services they provide.

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[104] AT&T Inc., Form 10-K for period ending 12/31/2009, filed February 25, 2010. Verizon Communications Inc., Form 10-K for period ending 12/31/2009, filed February 26, 2010.
[105] Centurylink Inc., Form 10-K for period ending 12/31/2009, filed March 1, 2010.
[106] FCC, *Telecommunications Industry Revenues: 2008*, released September 2010, at Table 10.
[107] FCC, *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, Fifth Order on Reconsideration and Order on Remand, 17 FCC Rcd 21274 (2002).
[108] *Global Crossing Telecommunications Inc. v. Metrophones Telecommunications Inc.,* No. 05–705. 2007.

E. Mandating discrimination among end-users

Perhaps unwittingly, many of the proposals in the NPRM would place LECs in one regulatory status if an end user may possibly have a substantial increase in demand for exchange access services and a different regulatory status if the end user may not. All common carriers, including LECs, are supposed to treat all current and potential customers and end users the same and in a non-discriminatory manner. It is likely inappropriate if not unlawful for a LEC to inquire about the expected future exchange access demand of an end user, and an end user would be presumably under no legal obligation to notify a LEC far in advance of an increase in demand. A LEC may file a tariff today and access demand may increase tomorrow without the advanced knowledge of the LEC. The NPRM does not address these situations.

Some of the proposals in the NPRM would create a different regulatory treatment for a LEC with changes in demand for access services and create substantial reporting requirements. Under the proposed regulatory system, a LEC may be tempted to shun—or treat differently--an end user that the LEC suspects might have an increased demand for exchange access services in the future. Increased access demand can lead to increased paperwork, administrative costs, and regulatory.

F. Obligations to small LECs rural America

Many of the LECs allegedly associated with traffic stimulation are small LECs in rural America. The Communications Act has a different and preferential treatment of telecommunications services offered in rural America, particularly as expressed in Section 214(e) and 254.[109] Rural telephone companies are even separate and defined entities under the Act,[110]and they have a privileged position under the Act.[111] The NPRM does not recognize either

[109] See, e.g., 47 U.S.C. 214(e), 47 U.S.C. 254, and 47 U.S.C. 309.
[110] 47 U.S.C. 153(37).

rural America or rural telephone companies, much less their unique status in communications law.

G. A deregulatory solution

Throughout the NPRM, the Commission addresses a purported problem, access stimulation, and addresses possible solutions all of which involve additional regulation. In promulgating rules under Section 204(a)(3), the Commission in 1997 clearly recognized that the purpose of the section as well as the entire Telecommunications Act of 1996 was deregulation.[112] It would be unfortunate if 13 years later the Commission were to examine tariff requirements for LECs and see only solutions that involve more regulation. Deregulatory solutions are available, such as noted earlier the clarification that IXCs may pass along exchange access charges to their customers.

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[111] See e.g., 47 U.S.C. 251(f), 47 U.S.C. 253(f), and 47 U.S.C. 309.

[112] FCC, *Implementation of Section 402(b)(1)(A)of the Telecommunications Act of 1996*, Report and Order, 97-23, January 31, 1997.